

SECRET

U.S.-EUROPEAN ECONOMIC RELATIONS

AN OVERVIEW

NSC Review Completed.

ISSUES

The confluence of a number of contentious issues in U.S.-EC economic relations has produced strong reactions in Europe. Key among these issues are: (1) the decision to extend extraterritorially the sanctions on oil and gas equipment and technology; (2) Commerce preliminary determinations on European steel subsidies; and (3) U.S. complaints against EC agricultural subsidies in the GATT (General Agreement on Tariffs and Trade).

These disputes threaten to color overall U.S.-EC relations, despite earlier progress in a number of areas -- including agreement at the Versailles Summit on future economic policy consultations, a study of the effect of past exchange rate interventions, and a narrowing of the gap on North-South issues. We have also recently achieved EC agreement to an extension of the international arrangement on export credits, including substantial increases in export credit rates for the Soviet Union.

The European nations are generally united in their strong opposition to the oil and gas equipment decision, but differences exist within the Community on both the steel and agriculture issues. As the United States has moved to challenge subsidy practices in international trade and as the current confrontation with the EC in steel has developed, the EC continually has attempted to discuss our bilateral trade relations in the broader context of U.S.-European security and political issues. Prior to the pipeline decision, U.S. representatives had some success in limiting this linkage, and in persuading the EC that the issues should be managed individually through the proper GATT and OECD mechanisms.

The Europeans also have argued that the oil and gas equipment decision casts doubt on the Summit process and consultations generally between the U.S. and its allies. The Heads of Government of the European Community have called for a genuine and effective dialogue with the United States and stated their determination to defend vigorously its legitimate interests in GATT. The Europeans have already announced their intention to distance themselves from the GATT Ministerial planning process in Geneva and have questioned the continuing utility of the Ministerial given current economic problems.

Unless the United States addresses these concerns, the Community may well be led to undertake specific retaliatory actions or to adjust its broader policies in GATT or elsewhere to conflict more sharply with U.S. objectives. Continued poor economic relationships can make it more difficult for us to gain and maintain the cooperation of our allies on security and diplomatic issues.

SECRET

SECRET

- 2 -

The poor state of the economies in both the United States and Europe has increased the political sensitivity on these economic issues in both Europe and the United States. The threat of protectionism, which lurks in the current economic environment, permits no hesitation in the Administration's policies to pursue specific as well as broad goals in GATT. Yet Europeans see our efforts to force an end to EC steel and agriculture subsidies which disrupt trade as confrontational and "kicking them while they are on their knees."

NATURE OF U.S. RESPONSE

In responding to this situation, U.S. policy should stress continuity, consistency, a low-key action-oriented approach, and above all, not raise expectations that cannot be fulfilled. Rather than being defensive or apologetic, we should approach the Europeans with a sincere desire to pick up on their appeal for a genuine and effective dialogue, pointing out that such a dialogue cannot continue to focus on U.S. policies alone.

In this broader context, the U.S. should distinguish among the various specific issues we face and the manner in which we proceed to address them. Where we have flexibility, we should also be more sensitive to timing of our decisions and announcements. Poor timing can give the appearance of a coherent anti-European policy where none exists.

Moreover, we should recognize that U.S.-EC differences on East-West trade issues will not be easily resolved. However, we can seek to establish an improved framework for U.S.-EC cooperation and mutual understanding and to maintain progress toward our basic economic objectives -- despite these differences -- if the EC is willing to divorce East-West disputes from other trade issues. This requires an EC recognition that we can have differences and still maintain an economic/political alliance.

1. On certain issues, such as East-West trade, sanctions, export credits, and economic policy coordination, we should proceed with a stress on the larger policy rationale.
2. On other issues, such as steel, agriculture, textiles, and various domestic actions that would benefit the allies, we should search for maneuvering room or flexibility, fully aware of the limits and of the desire not to raise expectations.
3. Finally, on the broadest issues of U.S. trade policy in GATT and U.S. policy toward the IMF and MDBs, the United States should maintain its leadership and continuity of policy, seeking to improve the operation of the international economic system. Obviously, our ability to find flexibility on the second group of issues above will support U.S. efforts to maintain its leadership and credibility on the long-term objectives.

SECRET

- 3 -

4. In making our individual decisions, we should be aware of the following upcoming events:

-- July 15	GATT Subsidies Code discussion of U.S. steel findings
-- July 21 - 22	OECD Steel Committee meeting
-- July 22	Possible Polish announcement of domestic policy changes
-- August 14	U.S. extension of pipeline sanctions takes effect
-- August 24	Deadline for final ruling by Commerce Department on steel CVD cases
-- September 6-9	IMF/World Bank meetings on economic policy consultations and intervention study
-- September 30	Expiration of U.S.-USSR grain agreement
-- November	GATT Ministerial
-- December	NATO Ministerial

SECRET